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Nos. 81-31, 81-228 and 81-455

IN THE

Supreme Court of the United States

October Term, 1981

STATE OF CALIFORNIA, *et al.*,

Appellants,

vs.

GRACE BRETHREN CHURCH, *et al.*,

Appellees.

On Appeal From the United States District Court for the Central District of California.

REPLY BRIEF OF APPELLANTS, STATE OF CALIFORNIA, CALIFORNIA EMPLOYMENT DEVELOPMENT DEPARTMENT, AND THE DIRECTOR OF THE CALIFORNIA EMPLOYMENT DEVELOPMENT DEPARTMENT.

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TABLE OF CONTENTS

Page

Preliminary Statement 1

Argument 3

I.

No Violation of the Free Exercise Clause Results From the Inclusion of Employees of Religious Schools in the Unemployment Compensation Tax Program 3

II.

No Violation of the Equal Protection or Religion Clauses Results From the Inclusion of Employees of Unaffiliated Religiously Oriented Schools in the Unemployment Compensation Tax Program 5

III.

No Violation of the Establishment Clause Results From the Inclusion of Employees of Religious Schools in the Unemployment Compensation Tax Program 7

Conclusion 12

TABLE OF AUTHORITIES

Cases — Page

Carmichael v. Southern Coal & Coke Co. (1937) 301 U.S. 495 7

Catholic Bishop v. NLRB (7th Cir. 1977) 559 F.2d 1112, aff'd (1979) 440 U.S. 490 ..... 8, 9, 10

Heffron v. Int'l. Soc. For Krishna Consc. (1981) __ U.S. __, 69 L.Ed.2d 298 11

Jones v. Wolf (1979) 443 U.S. 595 ..... 8, 11

Lemon v. Kurtzman (1971) 403 U.S. 602 7

Meek v. Pittenger (1975) 421 U.S. 349 7

Presbyterian Church v. Hull Church (1969) 393 U.S. 440 11

United States v. Dykema (7th Cir. 1981) 666 F.2d 1096 10

United States v. Lee, 50 U.S.L.W. 4201 (U.S. February 23, 1982) 1, 2, 3, 4, 5, 6, 7, 8

Constitution

United States Constitution, First Amendment 6, 9, 11

Statutes

United States Code, Title 26, Sec. 501(c)(3) 10

United States Code, Title 26, Sec. 1402(g) 2, 6

United States Code, Title 26, Sec. 3309(b)(1) 2, 4, 5, 6

United States Code, Title 26, Sec. 3309(b)(1)(B) 7

United States Code, Title 29, Sec. 160(c) 9

United States Code, Title 29, Sec. 160(e) 9

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REPLY BRIEF OF APPELLANTS, STATE OF CALIFORNIA, CALIFORNIA EMPLOYMENT DEVELOPMENT DEPARTMENT, AND THE DIRECTOR OF THE CALIFORNIA EMPLOYMENT DEVELOPMENT DEPARTMENT.

Preliminary Statement.

Subsequent to the filing of the opening briefs in the present matter, this Court's decision in *United States v. Lee*, 50 U.S.L.W. 4201 (U.S., February 23, 1982) was handed down. That decision is dispositive of much of the appellees'[1] arguments herein, particularly with respect to their Free Exercise and Equal Protection arguments.

In *Lee*, this Court rejected the Free Exercise arguments of an Amishman who contended that not only the payment of social security taxes, but also the receipt of social security

[1] "Appellees" includes the plaintiffs in both the Grace Brethren case and the Lutheran case.

benefits was directly prohibited by his religion. Although a more direct conflict between the Amish faith and the obligations imposed by the social security system existed in *Lee* than is present in the instant case, this Court concluded that the social security tax was constitutional as applied to the Amishman. In reaching its conclusion, this Court recognized that not all burdens on religion are unconstitutional and further that limitations on religious liberty may be justified if they are essential to accomplish an overriding governmental interest. *Lee, supra*, 50 U.S.L.W. 4201, 4203. This Court had little difficulty in finding such an overriding governmental interest due to the comprehensive nationwide nature of the social security system. *Ibid.* As this Court aptly noted, the unemployment compensation tax program involved herein is part of this comprehensive system. *Id.* at 4202, fn. 1.

In *Lee*, this Court also took note that Congress accommodated religious beliefs to the extent compatible with a comprehensive national program by providing for a limited exemption from social security taxes for self-employed Amish and others satisfying the criteria under 26 U.S.C. § 1402(g). *Id.* at 4204. This Court concluded that Congress' accommodation and resulting classification of employers was quite permissible. *Ibid.* The line Congress drew in 26 U.S.C. § 1402(g) provided for a "narrow category which was readily identifiable." *Ibid.* In the present matter, the State has demonstrated that a similar accommodation and classification was made by Congress in enacting the 26 U.S.C. § 3309(b)(1) exemption statute. *See*, State Amended Brief, pp. 31-35.

In all, this Court's decision in *Lee* is completely consistent with the State's position in the instant case and should provide compelling authority in the resolution thereof.

ARGUMENT.

I.

No Violation of the Free Exercise Clause Results From the Inclusion of Employees of Religious Schools in the Unemployment Compensation Tax Program.

As was noted above, this Court's decision in *Lee* effectively disposes of all the appellees' Free Exercise arguments. The interference with religious activity alleged by the appellees does not even approach the level of conflict which was present in *Lee*. Unlike the taxpayer in *Lee*, appellees do *not* contend that the payment of unemployment taxes and the receipt of unemployment benefits are prohibited by their religion. Rather, the appellees argue *inter alia* that the unemployment compensation tax program would impose an administrative and tax burden on the religious employers, would interfere with the right of the religious employers to employ who they wish, would interfere with parents' ability to choose a religious education for their children and would interfere with the opportunity of religious teachers to carry out their religious vocation, etc. *See*, Brief for Grace Brethren Church, pp. 28-36; Brief of Lutheran Church, pp. 26-32. Plainly, none of these alleged "burdens" is equal to or greater than the burden found in *Lee*. Moreover, as was pointed out in the State's Amended Brief, the injury to the Free Exercise rights of appellees is actually nothing more than the purely financial burden the program would impose upon them. *See*, State Amended Brief, pp. 27-30. In light of *Lee*, this "burden" is not enough to overturn a valid tax which is neutral in its general application.

The Grace Brethren appellees also contend that the unemployment tax is on a purely religious activity. *See*, Brief for Grace Brethren Church, pp. 28-31. The State respectfully disagrees. As in *Lee*, once the appellees have become

involved in an employer-employee relationship, they then have entered into a *commercial activity* and must abide by the rules governing others in that activity. *United States v. Lee, supra*, 50 U.S.L.W. 4201, 4204. It is irrelevant that one or both of the parties to the relationship are religious. It is still a commercial activity and may be subject to said rules.

Moreover, the Grace Brethren appellees' argument that the unemployment compensation tax program somehow results in an ongoing involvement between the employer and the State is extremely misleading. *See*, Brief for Grace Brethren Church, pp. 22, 34. Contrary to their assertions, there are no entry audits or continuing inspections required under the law. In fact, if the religious employer elects the reimbursement method of contribution, its contact with the State would indeed be minimal since no taxes are owed unless unemployment benefit claims are filed by and unemployment benefits are paid to its discharged employees. Allowing the religious employers the right to use the reimbursement method was an attempt by Congress to accommodate the religious beliefs of these employers. *See*, State Amended Brief, pp. 28, 33-35.

Finally, as was noted above, there is indeed a compelling governmental interest in providing a comprehensive nationwide unemployment insurance program. *See, United States v. Lee, supra*, 50 U.S.L.W. 4201, 4203; State Amended Brief, p. 30. As in *Lee*, there is broad public interest in maintaining a fiscally sound tax system which would be severely jeopardized by extending the exemption provided in 26 U.S.C. § 3309(b)(1) to the non-church affiliated appellees involved herein.

II.

No Violation of the Equal Protection or Religion Clauses Results From the Inclusion of Employees of Unaffiliated Religiously Oriented Schools in the Unemployment Compensation Tax Program.

Both the Grace Brethren appellees and the *amicus curiae* argue that it is unconstitutional to deny the exemption to religious organizations which are unaffiliated with a church while allowing church-affiliated organizations to be so exempt. The State has demonstrated that this argument is devoid of merit. *See*, State Amended Brief, pp. 31-35. This Court's decision in *Lee* provides additional persuasive authority in support of the State's contentions.

As was previously pointed out, the decision in *Lee* indicates that there is *no* constitutional right to a tax exemption for the religious employer. Congress is permitted great latitude in classifying employers as exempt or non-exempt. Accordingly, this Court in *Lee* applied the strict standard regarding tax exemptions in general and held that "the tax imposed on employers to support the social security system must be uniformly applicable to all, *except as Congress provides explicitly otherwise*." *United States v. Lee*, *supra*, 50 U.S.L.W. 4201, 4204. A similar standard is compelled in the instant matter as well.

As in *Lee*, Congress has confined the 26 U.S.C. § 3309(b)(1) exemption to a narrow category which is readily identifiable — churches and religious organizations which are controlled by churches. In the State's Amended Brief, the legislative history behind the 26 U.S.C. § 3309(b)(1) exemption was examined. *See*, State Amended Brief, pp. 33-35. The history indicates that although Congress recognized that low unemployment generally existed in religious organizations, Congress was concerned with the fact

that unemployment still affected a substantial number of their employees.[2] Therefore, Congress attempted to accommodate religious organizations in much the same way as it did under 26 U.S.C. § 1402(g). In fact, Congress not only continued the exemption from federal unemployment taxes for all religious organizations as well as the exemption from state unemployment taxes for churches and church affiliated organizations, but also further accommodated non-church affiliated religious organizations by permitting them to use the reimbursement method of contribution with respect to state unemployment taxes.

The argument put forth by the Grace Brethren appellees and the *amicus curiae* that church affiliated employers and non-church affiliated employers have equal status under the First Amendment and therefore both must be exempt from unemployment taxation is effectively answered by the decision in *Lee*. Although there is virtually no difference in status under the First Amendment between self-employed Amish and non-self-employed Amish, this Court in *Lee* sustained the limitation of the exemption to the former alone. A similar result is mandated here as well.

In its Amended Brief, the State also pointed out that the line drawn between churches and non-churches in 26 U.S.C. § 3309(b)(1) avoids excessive governmental entanglement with religious entities. *See*, Amended Brief, pp. 31-35. It keeps the State out of the business of evaluating the relative

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[2]Congress was obviously cognizant of the fact that unlike social security retirement benefits and disability benefits, it would be less likely for a religious employer to provide on its own unemployment benefits for a discharged employee. Indeed, in the instant case, there is testimony that Redwood Christian Schools has its own disability program, but *no* evidence that it would institute its own unemployment program if it was not required to participate in the federal-state program. (*See*, R.T. pp. 50-52 — R.T. refers to Reporter's Transcript of proceedings before Honorable Mariana R. Pfaelzer on August 12-13, 1980.)

merits of differing religious claims. *See, United States v. Lee, supra*, 50 U.S.L.W 4201, 4204, fn. 2. (Stevens, J., concurring); *see also, Carmichael v. Southern Coal & Coke Co.* (1937) 301 U.S. 495, 512-513. (Exemption of particular classes of employers may be explained by administrative convenience or fear of constitutional restrictions). Plainly, if there was to be an exemption at all, a line had to be drawn somewhere. Without a clear demarcation, a significant potential for abuse would arise, because any entity choosing to call itself religious could be exempt simply by virtue of that choice. The line drawn by Congress strikes a reasonable balance between sincerely held religious beliefs and protection for employees against unexpected wage loss.[3]

III.

No Violation of the Establishment Clause Results From the Inclusion of Employees of Religious Schools in the Unemployment Compensation Tax Program.

The appellees go to great lengths in their briefs in attempting to demonstrate the potential for excessive entanglement in the benefit eligibility determination process. However, upon close scrutiny of the Grace Brethren appellees' "thirteen points of entanglement" and the Lutheran appellees' similar assertions, it becomes evident that the alleged entanglement objected to by both is merely whether the religious employer can be forced to prove that an established work rule existed and that it was knowingly violated by the employee. In essence, the appellees are arguing

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[3]The determination under 26 U.S.C. § 3309(b)(1)(B) of whether a religious school, which is operated, supervised or controlled by a church or association of churches, is operated primarily for religious purposes, is effectively controlled by this Court's decisions in *Meek v. Pittenger* (1975) 421 U.S. 349, 365-366 and *Lemon v. Kurtzman* (1971) 403 U.S. 602, 613-618. Notwithstanding the Grace Brethren appellees' assertions to the contrary, that determination is quite dissimilar to the determination of whether a school has a sufficiently religious mission or curriculum content.

that they cannot be constitutionally forced to do anything by the government. However, as this Court indicated in *Lee*, this is simply not the case once a commercial activity, in this instance an employer-employee relationship, is entered into. The appellees must abide by the rules governing others in that same activity. Furthermore, as was shown in the State's Amended Brief, the precise type of inquiry required in benefit eligibility hearings is permissible under the standards set forth in the church property cases decided by this Court. *See*, State Amended Brief, pp. 21-27. In particular in *Jones v. Wolf* (1979) 443 U.S. 595, this Court held that it was constitutionally permissible to require the interested parties to modify the deeds, charters or church constitution in order to ensure that a certain result would be reached by the civil courts adjudicating the dispute. *Id.* at 606. The burden involved in taking such steps was held to be minimal. *Ibid.* Civil courts would be bound to give effect to the result indicated by the parties, provided it is embodied in some legally cognizable form. *Ibid.* Consistent therewith, it would not be an unconstitutional burden to require the religious employer to put its work rules in a legally cognizable form if it wished to ensure a particular result in a benefit eligibility hearing.[4]

The appellees rely heavily on *Catholic Bishop v. NLRB* (7th Cir. 1977) 559 F.2d 1112, aff'd (1979) 440 U.S. 490, as support for their contentions that unconstitutional entan-

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[4]It is in this light that Grace Brethren appellees' reference to a benefit eligibility hearing in which the phrase "attending church regularly" was interpreted by the Administrative Law Judge must be viewed. *See*, Brief of Grace Brethren Church, p. 16. Had the employer specifically defined "regularly" and set forth the definition in a legally cognizable form which was established and known to the employee, the employer could have ensured the rejection of the discharged employee's claim for unemployment benefits.

glement exists in the benefit eligibility determination process. Their reliance is misplaced for several reasons.

To begin with, although the Seventh Circuit in *Catholic Bishop* concluded that an NLRB attempt to exercise its broad jurisdiction over diocesan schools to determine whether a particular personnel practice constituted unfair labor practices, would foster excessive governmental entanglement, this Court declined to decide the First Amendment question. Nevertheless, there are a number of facts which distinguish the situation in *Catholic Bishop* from the present case.

In *Catholic Bishop*, the issue involved mandatory collective bargaining which by its own nature would affect the development of curriculum, faculty standards, working conditions and other aspects of school operations. The unemployment compensation tax program would not necessitate any ongoing governmental involvement in any of these or other areas and in fact would not even come into play until an employee had been terminated and was no longer connected in any way with a particular school. In addition, the financial impact of the unemployment compensation tax program cannot be compared with the financial ramifications of NLRB jurisdiction over diocesan schools. Unlike the unemployment compensation tax program, the NLRB has the power to order reinstatement of employees with back pay and to utilize judicial authority to enforce its rulings. *See*, 29 U.S.C. § 160(c), (e). Finally, unlike the present case where there is only speculation that benefit eligibility hearings which necessitate an inquiry into church doctrine might occur, there was *actual* proof of unfair labor practices

in *Catholic Bishop*. In all, *Catholic Bishop* is simply not supportive of appellees' position herein.[5]

The appellees have also argued that the State is attempting to improve the trial record, specifically regarding the testimony of Mr. Streett and Mr. Carter. This is simply not the case. The State is only suggesting that the federal witnesses' testimony be closely scrutinized. Upon such a review it can be seen that in addition to no actual proof of excessive entanglement existing herein, the federal standards to be used in benefit eligibility hearings are in fact *neutral secular* standards which are to be used in all situations. Indeed, there was testimony that *no* specific guidelines or standards exist for religious employers. *See*, R.T. pp. 175, 232. These *neutral secular* standards are identical to the standards set forth under California law. That is, in a benefit eligibility hearing, the employer has the burden of proving that an established work rule was knowingly violated. *See*, State Amended Brief, pp. 21, 24. Consequently, regardless of whose burden it is to show either the potential for excessive governmental entanglement or the

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[5]The Seventh Circuit recently distinguished *Catholic Bishop* in a case involving the enforcement of an Internal Revenue Service summons relating to the determination of entitlement to a tax exemption for a church. In *United States v. Dykema* (7th Cir. 1981) 666 F.2d 1096, the Court held that in determining whether a church is operated exclusively for religious purposes (26 U.S.C. § 501(c)(3)), it is necessary and proper for the Internal Revenue Service to survey *all* activities of the organization and to evaluate said activities by the use of *objective criteria*. *Id.* at 1100. Further, the Court concluded that such an evaluation would not require the Service to enter into a subjective inquiry with respect to religious truth which would be forbidden by the First Amendment. *Ibid.* Finally, the Court stated with respect to *Catholic Bishop*:

> "Clearly also there is no continuing supervision or regulation of the religious mission of the organization such as was condemned in *NLRB v. Catholic Bishop of Chicago* (citation omitted)." *Id.* at 1100, fn. 5.

The Seventh Circuit's conclusions are entirely appropriate herein as well.

absence thereof, the conclusion is inescapable that no potential for excessive governmental entanglement has been demonstrated.

Finally, in response to the State's use of the church property cases, the appellees attempt to equate the benefit eligibility determination process wherein it is decided whether an employee knowingly violated an established work rule, to the weighing and interpreting of church doctrine prohibited in *Presbyterian Church v. Hull Church* (1969) 393 U.S. 440. In doing so, the appellees ignore the crucial distinction between examining church documents to determine how the parties decided to govern a particular religious organization and actually determining what the true faith is. The former is permissible under the *Jones v. Wolf* standard. Similarly, it is constitutionally permissible for the State to determine whether the employee knew of the work rule he allegedly violated. *See*, State Amended Brief, pp. 24-25. In effect, a religious employer cannot label everything "doctrine" and thereby foreclose any governmental contact with the commercial activities of the employer. *See, Presbyterian Church v. Hull Church, supra*, 393 U.S. 440, 453 (Harlan, J., concurring); *Heffron v. Int'l. Soc. For Krishna Consc.* (1981) ____ U.S. ____, 69 L.Ed.2d 298, 309. As the State pointed out in its opening brief, the benefit eligibility hearing is closely analogous to a breach of contract adjudication in that the employer is in essence alleging the employee knowingly violated his or her "contract of employment." *See*, State Amended Brief, p. 26. The adjudication is and can be conducted under a neutral principles approach. As such it is quite permissible under the First Amendment.

Conclusion.

For the reasons heretofore stated, the judgment of the District Court insofar as it is challenged by the State's appeal should be reversed.

Respectfully submitted.

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